***United States Court of Appeals***

***for the Second Circuit***

# REPLY BRIEF

# 75-7284



## United States Court of Appeals
FOR THE SECOND CIRCUIT

LAWRENCE R. BARNETT, C. LEONARD GORDON and ALFRED L. HOLLENDER,

*Plaintiffs-Appellants,*

*against*

DON KIRSHNER, IRVING COHEN, HERBERT T. MOELIS and KIRSHNER ENTERTAINMENT CORPORATION,

*Defendants-Appellees.*

ON APPEAL FROM THE UNITED STATES DISTRICT COURT SOUTHERN DISTRICT OF NEW YORK

## REPLY BRIEF OF THE PLAINTIFFS-APPELLANTS

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Defendants-Appellees.

Docket No. 75-7284

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# PLAINTIFFS-APPELLANTS' REPLY BRIEF

## INTRODUCTION AND SUMMARY OF ARGUMENT

In our main brief, we showed that defendants deceived plaintiffs, their co-venturers in a close corporation, by buying up their shares while secretly and simultaneously obtaining valuable properties for the company. The central issue in the case turns upon whether certain "consents" formed a part of the sales transactions. If they did, the trial court held (and defendants concede) they were conditions precedent which were not timely met, and thus defendants' omissions to disclose material facts were in connection with their purchases of plaintiffs' stock.

As shown below, defendants' brief, contending that the consents were not a part of the transaction, disregards the facts proved at trial and cites authority irrelevant to

the facts of record.

ARGUMENT

POINT I

DEFENDANTS' MATERIAL OMISSIONS WERE IN CONNECTION WITH THEIR PURCHASES OF PLAINTIFFS' SECURITIES

a) The Omission To Mention The Lerner Negotiations Was Material.

The defendants conceded (Tr. 299), and the trial court correctly found that the non-disclosure of the Lerner negotiations was material and a violation of the Securities Law if in connection with the sale of plaintiffs' securities. Defendants have not disputed this holding on this appeal.

b) The Omissions Were In Connection With The Sale As A Matter Of Contract Law.

The Court went on to hold that the omissions were in connection with the sales if the consent forms are found to be a part of the sales, constituting a condition precedent.

Now, two interpretations of that transaction are being contended for.* Defendants say that the sales were

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* Defendants do not dispute that the trial court's holding, based on documentary evidence, is freely reviewable on appeal. Shiya v. National Committee of Gibran, 381 F.2d 602,606 (2d Cir. 1967), cert. denied, 389 U.S. 1048 (1968)

completed as to plaintiffs Barnett and Gordon by December 30, 1968, and as to Hollender by January 29, 1969, and that the consents were not an integral part of the sales contract. (Def. Br. p. 11) Plaintiffs contend that the consents were an integral part of the transaction, and operated as a condition precedent to the sales. However, in making their argument, defendants have failed to take account of the facts. Accordingly, the authority cited in their brief is completely inapposite to the case.

(i) The Purpose Of The Consents.

Plaintiffs' interest in KEC was more than the mere ownership of stock. The plaintiffs were obligated, pursuant to the shareholders agreement, to make certain loans when called to do so by the corporation. The obligation was evidenced by demand notes in amounts proportionate to their shareholdings. (Ex. 1, p. 6). Plaintiffs wanted to get out of their obligations to make further loans. Indeed, their desire to avoid this liability was the central reason for selling their shares. (85a, 92a, 138a) Defendants were willing to assume those obligations (123a, 127a, 135a). The non-selling shareholders were entitled to have solvent, responsible persons under contract to make those loans. It is in this factual setting that the sales agreements must be considered.

The purpose of the consent was, first, to shift the obligation to make further loans from the plaintiffs to the defendants, and second, to obtain the concurrence of the non-selling shareholders to that switch. The consent forms (addressed to both the selling plaintiffs and non-selling shareholders) recite:

> "To induce you to permit me to purchase all of the common stock of Entertainment, DKMI and of KEC owned by ________________ and to arrange to lend to Entertainment the sum of $__________ on the same terms and conditions as the said loan by ____________, I hereby agree, effective from the date on which such purchase shall be completed, to become and be bound by each of the Agreements as if I had been named therein at the time of their original execution. Effective from such date, each of you releases ____________________ from any and all liability under the Agreements."* (123a, 129a, 135a)

Thus the consents were tri-partite agreements between the buying defendants, the selling plaintiffs and the non-selling shareholders. This is further evidenced by the fact that plaintiffs were asked to, and did, sign these consents along with the other documents of sale. Defendants' brief repeatedly misstated this central fact, by asserting that the consents were between defendants and the non-selling shareholders

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* The agreements follow the same form for all selling plaintiffs. The names of the selling plaintiffs and the amounts of their loans were inserted in the appropriate blanks.

(Def. Br. p. 12-15). To argue that the consents were no part of the transactions by which plaintiffs terminated their interest in KEC ignores the plain intent and purpose of the consents. Defendants have completely failed to meet this point, or to explain in any way the plain meaning of the consent contracts.

(ii) <u>The Effect Of The Consents</u>.

The consents provide that all of the non-selling shareholders must agree to the shifting of contractual obligations from selling plaintiffs to the buying defendants. The consents specify that unless all consents are received (and thus the transactions are all completed) prior to March 1, 1969, the transactions would be "null and void." The provision for a deadline protects the selling plaintiffs from the possibility that they would <u>indefinitely</u> be liable for further loans during the period while consents were being solicited. The provision <u>voiding</u> the transactions after the deadline, prevents the plaintiffs from the absurd result of having parted with the stock (and thus the opportunity to share profits of the enterprise) while still being obligated to make further loans. The fact is, that the deadline came and went without the consents being obtained. Plaintiffs had no way of knowing this as the consents were to be collected by Defendant Cohen's law firm. After March 1, 1969, the sales transactions were void, and plaintiffs were entitled to withdraw their

consents. Defendants have completely failed to address this point in their brief.

Defendants make much of the fact that the money had been exchanged and that plaintiffs had not segregated the funds (Def. Br. p. 13). These facts are of no legal significance. See Detroit Football Company v. Robinson, 186 F.Supp. 933 (E.D.La.) aff'd 283 F.2d 657 (5th Cir. 1960), cited in our main brief at page 24, and nowhere distinguished by defendants. Robinson signed a contract with the Detroit Lions which provided that it would become binding only if it were approved by the Commissioner. He was then given a cash advance by Detroit. Some time after this, and before the Commissioner had given his approval, Robinson signed with another team, notified Detroit and tendered back the money to them. The court ruled that the Commissioner's approval was a condition precedent to the very existence of a contract; that this condition had not been met, and that the payment to Robinson "must be viewed as given conditionally, on the contingency that a binding contract would later come into existence." 186 F.Supp. at 935.

(iii) Defendants' Authority Is Not In Point.

The authority cited by defendants (Def. Br. p. 15) is inapposite as it holds no more than that title may pass where the parties intend that it pass. Here, the facts ne-

gate any such intention. Defendants' further argument (Def. Br. p. 15) that only the non-selling shareholders had a right to attack defendants' title (and the cited authority) is irrelevant. The consents were addressed to, and signed by plaintiffs, and protected their interests as well as those of the non-selling shareholders (See pp. 3-5, supra). The condition precedent not having been met, plaintiffs were free of the sales contracts.

(iv) Defendants' Argument Results In An Absurdity.

Defendants argue, at p. 13 of their brief, that the consents were no part of the sales transactions, but that instead, plaintiffs breached the shareholders agreement, while defendants set up the consents to protect their title to the shares (Def. Br. p. 16). In order to read the consents out of the sales transaction in this way, we would have to assume a) plaintiffs intended to breach the shareholders agreement; b) defendants (fiduciaries because of their position as control group and counsel to the close corporation, KEC) either willfully induced or aided and abetted such a breach of the shareholders agreement, or willfully overreached and took advantage of plaintiffs and set up the transaction so that plaintiffs had no legal protection, but defendants were covered.

The obvious conclusion is that neither defendants

nor plaintiffs intended any such result.* The only natural reading of the agreement is that the consents were conditions precedent to the sales so that all parties -- plaintiffs, defendants, and non-selling shareholders -- were protected. It has long been the law that as between two otherwise reasonable interpretations preference is given to the one that will make the agreement lawful and valid. Corbin on Contracts, §§545 et. seq.

(v) The Omissions Were In Connection With The Sales As A Matter Of Securities Law.

In our main brief, we argued that the District Court's ruling unnecessarily restricts the prophylactic purpose of the Federal Securities Laws' disclosure requirements. We pointed out that until the consents were given, plaintiffs were for many purposes still the owners of the stock and liable to make further loans; and that plaintiffs were entitled to withdraw their consents after March 1, 1969. Without the information withheld from them by defendants, plaintiffs were deprived of the exercise of knowledgeable consents. Thus, plaintiffs are entitled to the protection of the Securities

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* Defendants argue (Def. Br. p. 13) that plaintiff Gordon never considered the effect of the consent letters. However, the contract, which was prepared by the defendants, speaks for itself, and its legal effect need not have been considered by Gordon. It is plain, however, that Gordon did not intend to breach the shareholders contract. Defendants do not argue otherwise, nor is there anything in the record that suggests otherwise. (Tr. 178-80)

Exchange Act. See, Champion Home Builders v. Jeffress, 490 F.2d 611 (6th Cir.), cert. denied, 416 U.S. 986 (1974). In Champion, the court held the date of a purchase of stock for purposes of Sec. 16(b) of the Securities Exchange Act to have been the date when the directors approved the purchase, rather than the earlier date when the shares were exchanged for value, as the incidents of ownership did not attach until the latter date, and the prophylactic purposes of the act were better served.

Defendants have not responded to these arguments, or attempted to discuss the authority cited.

## POINT II

### CONCEALMENT OF THE IDENTITY OF THE PURCHASER OF PLAINTIFF HOLLENDER'S SHARES WAS FRAUDULENT

Defendants' authority is not in point. Defendants argue (Def. Br. p. 7) that the identity of a purchaser of stock is not material, citing Ross v. Licht, 263 F.Supp. 395 (S.D.N.Y. 1961). However, in that case, the court found the identity of the purchaser to be immaterial since the purchaser was one of the people to whom the selling plaintiff had been trying to sell his shares in the first place.

Here, however, Saltzman was definitely not a person to whom Hollender wished to sell his shares. Defendants ad-

mitted they had used the double nominee arrangement for exactly this reason. (40a-41a)

In addition, a reasonable man might well be influenced in his decision of whether or not to sell his shares by the fact that Saltzman, the producer of the James Bond films, and an extremely successful figure in the entertainment industry, had had a change of heart and had decided to buy into the venture after previously having refused to do so. (Tr. 120-121)

Defendants attempt to dismiss the fact that Hollender's suspicions would have been aroused by this change on Saltzman's part as "minor league Monday morning quarterbacking." (Def. Br. p. 18) However, where, as here, defendants went to great lenghts to deceive Hollender, and thus obtain his stock, they should not now be permitted to argue that the deceit was not material. Where such deliberate deceit is perpetrated on a seller by an insider buyer, the court should view with suspicion arguments by the deceitful insiders that their deceit was immaterial.

## C O N C L U S I O N

For the reasons given, the judgment of the District Court should be reversed, and judgment should be entered for the plaintiffs.

Respectfully submitted,

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**AFFIDAVIT OF SERVICE**

STATE OF NEW YORK,
COUNTY OF NEW YORK, ss.:

Juan A. Delgado , being duly sworn, deposes and says that he is over the age of 18 years, is not a party to the action, and resides at 596 Riverside Drive, New York
That on August 29, 1975 , he served 2 copies of Reply Brief of the Plaintiffs-Appellants
on

HARRIS FREDERICKS & KROBKIN, ESQS.,

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by delivering to and leaving same with a proper person or persons in charge of the office or offices at the above address or addresses during the usual business hours of said day.

Juan A. Delgado ..........

Sworn to before me this
29th day of August , 19 75

Charles J. Esposito

CHARLES J. ESPOSITO
Notary Public, State of New York
No. 30-1132025
Qualified in Nassau County
Commission Expires March 30 1977